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No. 84-1076

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

TRANSCONTINENTAL GAS PIPE LINE CORPORATION,
Appellant,

VS.

THE STATE OIL AND GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, INC., *et al.*,
Appellees.

On Appeal from the Supreme Court of Mississippi

REPLY FOR APPELLANT

JOHN MARSHALL GROWER
(Counsel of Record)
JEFFERSON D. STEWART
R. WILSON MONTJOY, II
BRUNINI, GRANTHAM, GROWER & HEWES
1400 First National Bank Building
Post Office Drawer 119
Jackson, Mississippi 39205
Telephone: (601) 948-3101

R. V. LOFTIN, JR.
THOMAS E. SKAINS
DAVID A. GLENN
TRANSCONTINENTAL GAS PIPE LINE CORPORATIION
Attorneys for Appellant

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

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REPLY FOR APPELLANT

This brief is submitted by Transcontinental Gas Pipe Line Corporation (Transco) to a limited number of the points raised in the Motions to Dismiss filed by the State of Mississippi, Getty Oil Company and Coastal Exploration, Inc. Since the majority of the points raised by Appellees have been addressed in Transco's Jurisdictional Statement and in the briefs filed by amici curiae, the United States of America and the Associated Gas Distributors, further response will not be made herein.

1. Appellees have argued that this Court should return to its approval of ratable take regulations in *Cities Service Gas Company v. Peerless Oil & Gas Company*, 340 U.S. 179 (1950) (hereinafter cited as *Peerless*). This position is incorrect.

In *Peerless*, this Court expressly noted that the issue of preemption, *i.e.*, possible interference with the federal regulatory scheme under the Natural Gas Act, had been neither raised nor decided, 340 U.S. at 188-89. *Peerless* is not a preemption case and therefore cannot support Appellees' position on the Supremacy Clause. This Court has never approved state ratable take regulations where a preemption challenge has been made. In fact, the only case which has considered state ratable take regulations in light of the Natural Gas Act was *Northern Natural Gas Co. v. State Corporation Commission*, 372 U.S. 84 (1963). Contrary to representations by Appellees, *Northern Natural* did not approve *Peerless*—it distinguished Peerless on the ground that the issues in the two cases were unrelated. *Id.* at 91, n. 10.

2. Appellees have asserted that the "deregulation" of the first sale of certain categories of natural gas under the NGPA was not only a withdrawal of FERC jurisdiction but also an open invitation for the substitution of a state regulatory scheme. This is incorrect in several respects. First, FERC has retained jurisdiction over interstate pipelines, their transportation of gas and their resales. For example, the "guaranteed" pass through for deregulated gas is still subject to FERC review and rejection based upon fraud, abuse or similar grounds, 15 U.S.C. Section 3431(c)(2). Therefore, federal domination of this field is still so complete that it precludes state regulation.

Second, state regulations which cause increased consumer gas prices are contrary to Congressional intent. One critical problem addressed by the NGPA was that earlier government control of wellhead prices had made those prices unresponsive to market conditions. Federal price controls had undervalued natural gas, creating high demand but discouraging adequate exploration. By "deregulating" prices, Congress did effect a limited withdrawal of FERC jurisdiction. The Congress recognized that an increase in consumer prices was a necessary evil in order to encourage production of adequate supplies. By eliminating federal control of wellhead prices, it was hoped to make those prices more responsive to the market.

Congress never anticipated that the production incentives of the NGPA would ultimately result in a severe oversupply of gas at above-market prices. However, it is completely inconsistent with the purpose of the NGPA to allow the states to enact regulations which have the practical effect of further increasing the price of gas to the interstate consumer. Federal "deregulation" of the price paid for the first sale of certain categories of natural gas was an indication that the price should remain unregulated and free to rise and fall with market conditions. *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 383-84 (1983). Deregulation was not an invitation to the states to re-regulate and thereby affect the price of gas.

3. Appellees also claim that there is no significant interstate impact of Rule 48 because the only adverse result is the imposition of take or pay obligations which can be "made up" by additional pipeline takes in later years. However, the impact is much broader. Appellees have generally ignored the "practical effects" of Rule 48. They have ignored the interstate burdens caused by forcing pipelines to purchase

more gas in Mississippi than from other states. They have likewise ignored the fact that ratable take regulations, if constitutional, can be expected to be enforced throughout Mississippi and in other states, resulting in a dramatic and adverse impact on the consumer. Finally, Appellees have ignored the consumer price increases resulting from taking additional quantities of deregulated gas, even at market value, in lieu of much older gas supplies which bear a contract price significantly lower than the current market value.

Appellees are likewise incorrect in their assertion that the impact of take-or-pay obligations does not create a Commerce Clause violation. Appellees disregard the increased price to consumers resulting from take-or-pay payments even if the gas is ultimately made up. Transco's only "profit" is the federally regulated rate of return it is given an opportunity to earn on its capital investment. Thus, the cost of take-or-pay, like the cost of higher gas prices, will be borne by the consumer through higher pipeline resale rates, thereby creating a Commerce Clause violation.

Further, the very existence of ratable take regulations helps assure that make-up will be an illusory remedy. Higher purchased gas costs and take-or-pay obligations increase the price of gas to the consumer, thereby further reducing market demand. As market demand decreases, less gas is sold, and more take-or-pay obligations are incurred. The date at which there is sufficient demand to make up gas is therefore delayed until after depletion of many wells and the expiration of contract make-up rights, rendering make-up impossible.

4. The State of Mississippi has asserted that Transco does not have standing to challenge Rule 48. A standing challenge is properly directed to a plaintiff in the federal

courts. *See, e.g., Warth v. Seldin*, 422 U.S. 490 (1975). The concept is simply inapplicable to a defendant like Transco, which merely defended itself against the application of an unconstitutional regulation and has appealed an adverse decision through the state courts to this forum.

5. Finally, Appellees have erroneously portrayed *Northern Natural* as based solely upon federal regulation of wellhead prices. *Northern Natural* was not concerned with wellhead prices; rather it dealt with ratable take regulations which indirectly conflicted with the federal regulation of pipelines and their transportation and resales of gas. 372 U.S. at 90-93. Federal jurisdiction over these areas remains even after the NGPA. *Exxon Corp. v. Eagerton*, 103 S. Ct. 2296, 2302-4 (1983); *Maryland v. Louisiana*, 451 U.S. 725, 749-52 (1981). Therefore, if there is to be regulation, it must come from the federal government. Just as in *Northern Natural*, state ratable take regulations intrude into an area reserved for the federal government and are therefore preempted.

CONCLUSION

Probable jurisdiction should be noted.

Respectfully submitted,

JOHN MARSHALL GROWER
(Counsel of Record)
JEFFERSON D. STEWART
R. WILSON MONTJOY, II
BRUNINI, GRANTHAM, GROWER
& HEWES

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